

ANALYSIS OF AMENDED BILL

Author: Klehs Analyst: Gail Hall Bill Number: AB 675
 Related Bills: See Legislative History Telephone: 845-6111 Amended Date: April 19, 2005
 Attorney: Patrick Kusiak Sponsor: _____

SUBJECT:

FTB Conduct Study of Revenue Impact Of, & Administrative & Implementation Issues
 With Requiring Certain Corporations To Calculate Tax Liability using Book Income As
 Annual Measurement of Income

SUMMARY

This bill would require the Franchise Tax Board (FTB) to conduct a study on a different method for taxing certain corporations.

SUMMARY OF AMENDMENTS

The April 19, 2005, amendments removed language that would have repealed provisions of current law relating to timber yield taxes and replaced it with the provisions discussed in this analysis. This is the department's first analysis of this bill.

PURPOSE OF THE BILL

The author's staff indicated the purpose of this bill is to authorize the FTB to study a new method of taxing corporations that would prevent the understatement of taxable income.

EFFECTIVE/OPERATIVE DATE

If this bill is enacted this session, it would be effective on January 1, 2006.

POSITION

Pending.

ANALYSIS**FEDERAL/STATE LAW**

Corporations use book income as the starting point for calculating federal taxable income and then apply the various federal tax adjustments to determine federal taxable income. Book income is calculated using accounting principals and is used for financial reporting purposes.

Generally, corporations use federal taxable income as the starting point for calculating state taxable income and then apply the various state adjustments. State adjustments are the differences between federal and state tax law.

Board Position:

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Department Director

Date

THIS BILL

This bill would require the FTB to conduct a study of the revenue impact of, and administrative and implementation issues with, requiring certain corporations to use book income, instead of federal taxable income, to calculate state income and franchise tax liability. This bill would require FTB to report the results of that study to the Legislature on or before June 1, 2006.

IMPLEMENTATION CONSIDERATIONS

This bill would not significantly impact the department's programs and operations.

PROGRAM BACKGROUND

Studies have shown a growing discrepancy between book income and taxable income. Book income is calculated based on accounting principals and is used to report the financial position of a corporation for creditors and shareholders. Officers of a corporation have incentive to overstate book income to enhance its financial position to its creditors and shareholders. This has resulted in some severely overstated financial income statements, such as those in the recent Enron and Worldcom scandals. On the other hand, the officers of a corporation also have an incentive to understate taxable income and thus reduce taxes, as seen in the widespread use of corporate tax shelters.

OTHER STATES' INFORMATION

Research conducted did not show that other states are conducting a study similar to the one described in this bill.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

This bill has no impact to state revenue since this is a study bill.

LEGISLATIVE STAFF CONTACT

Gail Hall
Franchise Tax Board
(916) 845-6111
gail.hall@ftb.ca.gov

Brian Putler
Franchise Tax Board
(916) 845-6333
brian.putler@ftb.ca.gov